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RUEHPE/AMEMBASSY LIMA 1078  
RUEHCV/AMEMBASSY CARACAS 0418  
RUEHBO/AMEMBASSY BOGOTA 1462  
RUEHRG/AMCONSUL RECIFE 3304  
RUEHRI/AMCONSUL RIO DE JANEIRO 7698  
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DEPT FOR WHA/BSC, WHA/EPSC, AND EB/OIA  
STATE PASS TO USTR FOR CRONIN/SULLIVAN  
STATE PASS EXIMBANK  
STATE PASS OPIC FOR MORONESE, RIVERA, MERVENNE  
NSC FOR FEARS  
USDOC FOR 4332/ITA/MAC/OLAC  
USDOC FOR 3134/USFCS/OIO  
USDOC ALSO PASS PTO/OLIA  
TREASURY FOR OASIA, DAS LEE AND JHOEK

AID/W FOR LAC/AA

E.O. 12958: N/A

TAGS: [EINV](#) [ETRD](#) [ECON](#) [EFIN](#) [BR](#)

SUBJECT: RECORD BRAZILIAN INVESTMENT OUTSIDE BRAZIL

SENSITIVE BUT UNCLASSIFIED; PLEASE PROTECT ACCORDINGLY

Summary

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1. (U) 2006 marked the first time in Brazilian financial history that Brazilians invested more overseas during the year than foreigners invested in Brazil. This phenomenon is due in large part to the internationalization of Brazilian companies, which are becoming global players as they search for ways to reduce costs and become more competitive. It also reflects Brazil's continued balance of payments surpluses in recent years. The Central Bank recently released figures projecting USD 18.3 Billion in Foreign Direct Investment (FDI) in Brazil in 2006, compared to a record USD 26 Billion in Brazilian Investment Overseas (IBD). Although a single multi-billion dollar transaction distorts these statistics to a degree, the overall trend is clearly towards greater Brazilian investment overseas. It's unclear what the overall impact of this will be on Brazil, a lower-middle income country that needs greater investment at home as well. End Summary.

2. (U) For the first time in its financial history, Brazilians and Brazilian companies are investing more overseas than the country is receiving in foreign investment. According to information from the Brazilian Institute of Geography and Statistics (IBGE), between January and September 2006 Brazilian investment overseas totaled USD 7.8 Billion, a 226 percent increase over the USD 2.4 Billion invested during the same period in 2005. Projections indicate that Foreign Direct Investment (FDI) in Brazil will close out the 2006 calendar year at approximately USD 18 Billion and Brazilian Investment Overseas (IBD) will exceed USD 26 Billion. This

turnaround was propelled by the recent USD 18 Billion acquisition of the Canadian mineral company Inco by Brazilian mineral giant Vale do Rio Doce, which is leading the way in internationalizing its investments, along with other Brazilian companies such as Petrobras, Gerdau Steel and Odebrecht (engineering and large construction projects). Petrobras, for example, invested USD 3.9 Billion overseas from January through September 2006, an increase of 110 percent over its 2005 foreign investment level for the same period.

#### Growing Brazilian Investment Overseas

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¶3. (U) Brazilian Investment Overseas (IDB) has been on the rise the entire year. Claudia Dionisio of the Office of National Accounts at IBGE observed that for the first time, this growth is not tied to the external balance of goods and services, but to the drop in external debt and the rise in interest rates for capital financing overseas. She added that since 2002, when Brazil began to have financing capability, the external balance was the principal component of growth. Although the positive external balance is no longer a principal component in generating GDP growth, it remains the principal component in generating the capacity for growth. Dionisio added that the main factor causing this upswing was the reaction to the lowering of the basic interest rate, which was 18 percent in 2005 but has since fallen to 13.25 percent. This reduced the attractiveness of domestic financial investments. Adriana Beringuy, also of the National Accounts Office at IBGE, observed that the rise in Brazilian financial activities overseas is related as much to trading of stocks and bonds as to the driving momentum of Brazilian companies in their desire to become more international.

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¶4. (U) The gross savings rate in relation to GDP has also registered high rates for the 3rd quarter at 25.2 percent, higher than the 24.3 percent in the same quarter of 2005. This is the best rate since 1995, with the exception of 3rd quarter 2004. Eustaquio Reis, an economist at the Institute of Applied Economic Research (Ipea), commented that the increase in both investment and savings rates are positive signs, but probably not sufficient to sustain a 5 percent growth rate in the economy for the coming year. According to Reis, the increase in savings is tied to the change in the balance of trade since 2000, when Brazil emerged from its trade deficit and began developing a surplus, which in 2006 is expected to be around USD 45 billion. He commented, "The business community produced more and then exported and saved the income it earned." For 2007, the Central Bank projects a 5 percent increase in Brazilian exports which should total 145 billion USD. Imports are projected to be USD 110 Billion, which will lead to a trade surplus of about USD 35 billion.

#### Foreign Direct Investment in Brazil

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##### Remains Strong

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¶5. (U) From January through November of 2006, FDI totaled USD 16.29 Billion, or the equivalent of 1.92 percent of GDP, with a performance that was better than forecast by the market. Even the Central Bank FDI registered 2.67 Billion for November 2006, more than double that of the same period in 2005. According to economist Sergio Vale of MB Associates, FDI in November was propelled by investment in the cellulose, paper and telecommunications sectors. The Central Bank showed that FDI in the cellulose and paper sector totaled USD 1.25 Billion in November 2006 while telecommunications totaled USD 780 Million. Altamir Lopes, Head of the Economic Department at the Central Bank, also was surprised at the results of November 2006 and projects that for December, the flow of foreign capital into Brazil will continue to grow, and should reach 2 Billion USD by the end of December. Thus, the Central Bank has adjusted its FDI projection for 2006 from USD 18 to 18.3 Billion, which will be a 20 percent increase over the USD 15 Billion in FDI in 2005.

¶16. (U) The success of Brazil's efforts to attract FDI has had a parallel effect on the amount of money remitted overseas. In November, remittances from Brazilian earnings and dividends sent overseas by multinational companies and foreign investors amounted to USD 763 million. For the year through November the amount was USD 13.27 Billion, compared to USD 10.44 Billion for the same period in 2005. Octavio de Barros, director of macroeconomic research at Bradesco Bank, stated that it is only logical that the more foreigners invest money in the country and the better their investments perform here, the more earnings they will have to send back to their home countries, thus raising the IBD amount.

#### Tourism Reflects Similar Investment Pattern

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¶17. (U) A greater amount of money flowing overseas from Brazilians is also reflected in the spending patterns of U.S and Brazilian tourists while on vacation. Through November of 2006, foreign tourists in Brazil spent USD 3.92 Billion, compared to 3.86 Billion in the same period of 2005, according to the Central Bank. The Ministry of Tourism states that this is a record for tourism spending. However, the spending of Brazilian tourists in the U.S. is even greater, with USD 5.25 Billion spent through November, as compared to 4.72 Billion in the same period of 2005. This accounts

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for a negative balance of 1.33 Billion in 2006 and 825 Million USD in 2005.

¶18. (U) The companies leading the Brazilian charge overseas have primarily, although not exclusively, been Brazilian commodity giants such as Companhia Vale do Rio Doce (CVRD), which is acquiring Canada's Inco mining in an 18 billion dollar deal. Gerdau Steel has made recent large acquisitions in the United States as well. These companies have been riding the recent commodity price boom and are flush with cash. But not all Brazilian overseas investment is by commodity firms, by any stretch of the imagination. In 2005, for example, Brazilian aircraft manufacturer Embraer established a facility in Harbin, China to assemble its strong-selling regional jets.

¶19. (U) Comment: Brazilian companies, in their quest for greater competitiveness and profit internationally, are increasing their investments outside Brazil. This increased investment has resulted in Brazil's annual overseas investments surpassing FDI in Brazil for the first time. Outgoing investment was strong throughout 2006, but received a major boost from the 18 Billion USD purchase of Canadian Inco mining company by the Companhia Vale do Doce Rio in the fall, perhaps signaling the beginning of a new wave of Brazilian companies expanding outside Brazil's borders to become international partners in the global economy. While a desire to expand overseas and diversify their investments no doubt drives many of these companies' decisions, there are also practical considerations such as seeking market access and cutting costs. Brazilian businesses, for example, often complain that the GoB's failure to pursue a free trade agreement with the U.S. hinders their efforts to access the U.S. market. They also complain loudly of restrictive labor rules and high taxes on the Brazilian economy. To some extent, their increased overseas investments also reflect these factors. End Comment.

¶19. (U) This cable was coordinated with Embassy Brasilia.

McMullen